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A FRENCH LAWYER LOOKS AT AMERICAN CORPORATION LAW AND SECURITIES REGULATION *

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How unwise on my part, when Dean Freedman was good enough to invite me to deliver the Owen J. Roberts Lecture, to have thought that I might speak on American corporation law and securities regulation. It is true that I have been fascinated by American securities law for a number of years. My attention was drawn to it by the publication in 1951 of Louis Loss's *Securities Regulation*.¹ The book, as you know, was immediately recognized as a landmark in this country. To me, it brought the discovery of an entirely new area of law. In France, we had some rather rigid rules on the issuance of shares, but at that time, nothing comparable to the requirements of the Securities Act of 1933.² Our disclosure rules were copied from a British statute dating from the turn of the century.³ We had no proxy regulation. And, of course, insider trading was not perceived as a problem because it was a practice enjoyed by every insider, to the benefit not only of himself, but of his relatives and friends. I tried to share my discovery of American securities law with my countrymen by publishing a long article

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¹ L. LOSS, *SECURITIES REGULATION* (1951). A second edition was published in three volumes in 1961, with a 1969 Supplement in three volumes.

² 15 U.S.C. §§ 77a-77bbbb (1976).

³ Companies Act of 1900, 63 & 64 Vict., ch. 48.

on the subject.⁴ Since that time, I have broadened my interest to include the study of American corporation law and English company law as well.⁵ I currently teach these subjects at the University of Paris I. One year, my students and I had the good fortune of having Professor William L. Cary as Visiting Professor, and we all learned a great deal from him. When Dean Freedman wrote to me, I thought it might be of interest to you to have the views of an outsider and to know what are, in his opinion, the strongest and also the weakest points of American corporate and securities law. Unfortunately, in preparing my lecture, I experienced two difficulties: first, if it is true that you have problems, those are problems for which French law normally provides no remedy; and, second, although I try to follow American law through books, legal periodicals, and personal contacts, my knowledge is essentially theoretical, while this audience includes well-known teachers and practitioners who know the subject much better than I do. I feel, therefore, that I have very little to offer you. I hope you will excuse me on account of my good will.

I should first perhaps reveal the source of my fascination for American corporation law and securities regulation. It is the extraordinary effervescence of your law and the unparalleled creativity and depth of your legal research. The fertility of your law had already struck, some twenty-five years ago, an English observer, Professor L.C.B. Gower.⁶ Your nation, with its fifty states and its federal government, is a unique laboratory for initiatives and experimentation. It has in addition an abundance of academics and able and aggressive practicing lawyers working both for the government and against it, and both for the corporations and against them, whose search for new ideas and new means of winning a case is sometimes stimulated by the prospect of a generous contingent fee. As a result of those permanent struggles between powerful forces that gather brain trusts to their support, and as a result of the originality and depth of disinterested scholarly writings, your body of law is clearly, in my opinion, the most advanced in the world. It is continually subjected to improvements, to new refinements, to changes, to self-questioning. As soon as a problem seems relatively settled, another arises. This subjection to various currents and

⁴ Tunc, *Le contrôle fédéral des sociétés par actions aux États-Unis*, 5 REVUE TRIMESTRIELLE DE DROIT COMMERCIAL 255, 509 (1952).

⁵ See Tunc, *A French Lawyer Looks at British Company Law*, 45 MOD. L. REV. 1 (1982).

⁶ Gower, *Some Contrasts Between British and American Corporation Law*, 69 HARV. L. REV. 1369, 1400 (1956).

cross-currents, however, also makes your body of law one of the most difficult in the world—probably the most difficult. It is perhaps the most sophisticated, with all the virtues and drawbacks implied by this description. This is true of American law in general. But this is true in particular of American securities regulation and corporation law. I shall consider these two fields of law separately, notwithstanding their increasing interconnections.

I. SECURITIES REGULATION

Securities regulation is typical of the advancement, complexity and subtlety of American law. I need not remind you of the pangs that section 16(b) of the Securities Exchange Act⁷ or rule 10b-5⁸ have inflicted on courts, lawyers, business people, and students. Although some problems have found their solutions in court decisions, it remains true now as in 1969 that “[s]ome engaged in the business of securities trading believe themselves to be characters from Victorian novels wandering aimlessly on treacherous moors.”⁹ One sympathizes with the businessman who, asked what he expects from his lawyer, answers: “I would like to know whether the chances of going to jail are 50-50 or 70-30 or 10-90!”¹⁰

Securities regulation is also a field in which comparison between American and French law does not suggest any possible improvement of the former. As a matter of fact, French securities law is almost entirely inspired by American law. Thirty-three years after you established the Securities and Exchange Commission, we created a *Commission des Opérations de Bourse* (currently called, by its initials, the COB), “to control the information of securities holders and the public on publicly held corporations and to see to the proper functioning of the stock markets.”¹¹ I confess having said some years ago that the COB could be compared to the SEC as a wheelbarrow can be compared to a Cadillac. Now, however, even though it may appear ridiculous to praise the COB on the home turf of the SEC, I am pleased to say that the COB, after a

⁷ 15 U.S.C. § 78p(b) (1976).

⁸ 17 C.F.R. § 240.10b-5 (1981).

⁹ *H. Kook & Co., Inc. v. Scheinman, Hochstin & Trotta, Inc.*, 414 F.2d 93, 98 (2d Cir. 1969).

¹⁰ *A Businessman's View of Lawyers*, 33 Bus. Law. 817, 819 (1978) (remarks by Donald N. Frey, Chairman of the Board of Bell & Howell Co.).

¹¹ Order No. 67-833 of Sept. 28, 1967, art. 1, 1967 *Dalloz-Sirey, Législation* [D.S.L.] 373, 1967 *Bulletin Législatif Dalloz* [B.L.D.] 659, 660.

slow start, has made excellent progress.¹² Every year the COB brings some improvement either to the law or at least to the practices of corporations, stock markets, accountants, or ancillary institutions like the financial press. The annual reports of the COB to the *Président de la République* bear witness to the progress made. The means of action of the COB are closely comparable to those of the SEC: rule-making, investigating, giving advisory opinions, requiring disclosure, persuading, cooperating with other financial institutions or professions related to the securities industry, suggesting legislative amendments, and educating the business community and the public. One might perhaps say that our ambition is to reach results as close as possible to the ones you have achieved with means that are perforce much more modest. The solicitation of proxies, for instance, must be accompanied by proper information. However, in order to reduce as much as possible the cost of such information for the corporations, the shareholder receives only the basic data necessary to reflect the situation and prospects of the corporation, plus a card by which he may request a more complete document.¹³

To appreciate at closer range the effectiveness of the COB, let us consider auditing. Auditing of accounts in France must traditionally be done by *commissaires aux comptes*. These are organs of the corporation.¹⁴ Their main duty is to report to the shareholders on the accounts. But they also perform a number of other important duties. They must report on contracts in which a director is interested, on any exception to the statutory preemptive rights of all shareholders in case of an increase in capital, on the issuance of bonds convertible into shares, and on a contemplated reduction of capital. Furthermore, if they discover some breach of the law, they must report it not only to the shareholders, but, if this breach constitutes a crime, to the public prosecutor (and our corporation legislation, in contrast with yours, contains a great number of criminal sanctions). They may even call the shareholders to a general

¹² See N. DECOOPMAN, *LA COMMISSION DES OPÉRATIONS DE BOURSE ET LE DROIT DES SOCIÉTÉS* (1980); Y. GUYON, *DROIT DES AFFAIRES* 453, 778 (1980); 1 R. ROBLOT, *TRAITÉ ÉLÉMENTAIRE DE DROIT COMMERCIAL DE GEORGES RIPERT* § 1206.1 (10th ed. 1980); 2 R. ROBLOT, *supra*, §§ 1852-1855 (9th ed. 1981).

¹³ Decree No. 67-236 of Mar. 23, 1967, art. 133, 1967 D.S.L. 137, 145, 1967 B.L.D. 235, 249.

¹⁴ See 2 J. HAMEL, G. LAGARDE & A. JAUFFRET, *TRAITÉ DE DROIT COMMERCIAL* §§ 673-685 (2d ed. 1980); 2 J. HÉMARD, F. TERRÉ & P. MABILAT, *SOCIÉTÉS COMMERCIALES* §§ 880-1063 (1974); 1 R. ROBLOT, *supra* note 12, §§ 1335-1359; Y. GUYON, *supra* note 12, §§ 357-391; P. MERLE & E. CHEVALLIER-MERLE, *L'APPLICATION JURISPRUDENTIELLE DE LA LOI DU 24 JUILLET 1966 SUR LES SOCIÉTÉS COMMERCIALES* §§ 305-334 (1976).

meeting if the directors fail to do so. Thus, the *commissaires aux comptes*, though they should not interfere in the management of the corporation, bear great responsibilities for the protection of the shareholders. To carry out their functions, they have the power to investigate the corporation's accounts and its financial situation, a power which extends to the parent company and its subsidiaries and even, to a certain extent, to any person who has been involved in any accounting operation for the corporation. They may seem significantly more powerful than the American auditors or the audit committees recently created. In the past, however, they did not actually exercise their functions.¹⁵ Some of them were satisfied to sign a short and insignificant paper prepared every year by their secretaries and pocket a fee that was negligible in relation to the task expected of them, but very reasonable in relation to what they had actually accomplished.

The picture has completely changed, partly as a result of the 1966 Act¹⁶ and the 1967 Decree,¹⁷ which are the basis of our corporation law, but mainly because of the influence of the COB. The COB obtained from the government the Decrees of August 12, 1969¹⁸ and December 7, 1976,¹⁹ which imposed a new structure and new regulations on the *commissaires aux comptes*.²⁰ The COB has also requested sanctions against the *commissaires* when necessary and has decided to ignore the signature of a *commissaire aux comptes* who has not fulfilled his functions. Thus the COB has greatly strengthened the institution and nearly transformed it. The 1969 Decree placed the profession under the permanent supervision of the COB. For instance, when someone is nominated for the position of *commissaire* of a publicly held corporation, he must inform the COB of his decision, and the COB may send the directors objections that should be forwarded to the shareholders.²¹ Further-

¹⁵ See Tunc, *L'effacement des organes légaux de la société anonyme*, 1952 Dalloz, *Chroniques* 73.

¹⁶ Statute No. 66-537 of July 24, 1966, 1966 D.S.L. 265, 1966 B.L.D. 353.

¹⁷ Decree No. 67-236 of Mar. 23, 1967, 1967 D.S.L. 137, 1967 B.L.D. 235.

¹⁸ Decree No. 69-810 of Aug. 12, 1969, art. 2, 1969 D.S.L. 320, 1969 B.L.D. 320.

¹⁹ Decree No. 76-1141 of Dec. 7, 1976, 1977 D.S.L. 4, 1976 Juris-Classeur Périodique [J.C.P.] III No. 45123, *modifying* Decree No. 69-810 of Aug. 12, 1969, 1969 D.S.L. 320, 1969 B.L.D. 320.

²⁰ See Y. GUYON & G. COQUEREAU, *LE COMMISSARIAT AUX COMPTES: ASPECTS JURIDIQUE ET TECHNIQUE* (1971); Guyon & Coquereau, *Le nouveau statut des commissaires aux comptes*, 1969 J.C.P. I No. 2290; Mabilat, *Le nouveau statut professionnel des commissaires aux comptes*, 88 REVUE DES SOCIÉTÉS 1 (1970); Mabilat, *Les modifications apportées au statut professionnel des commissaires aux comptes par le décret du 7 décembre 1976*, 1977 J.C.P. I No. 2835.

²¹ Decree No. 69-810 of Aug. 12, 1969, art. 64, 1969 D.S.L. 320, 324, 1969 B.L.D. 320, 324.

more, a *commissaire aux comptes* should keep a file of all documents received from each corporation he controls, all documents he has himself prepared, all tasks he has performed, and all moneys he has received. These files must be at the disposal not only of the organs of the profession and the public prosecutor, but also of the COB, which may ask the *commissaire* for explanations or justifications.²² Thus, the *commissaires aux comptes* have become truly effective instruments for the protection of shareholders.

Perhaps you will be skeptical of the performance of the COB if I now disclose that it works with a small staff of forty-seven professionals and forty-two clerical assistants. I assure you, however, that corporate directors and officers, accountants, *commissaires aux comptes*, stock exchange officials, the press, and others believe that it has become terribly efficient. This, of course, is not in the least a hint that the SEC could perform its job if trimmed down to this size!

One other point of comparison between American and French law may interest you: the regulation of insider trading. We did not do anything against insider trading until 1967, when we decided to fight it by borrowing your classic weapon against improprieties, disclosure. We were very clumsy in using it, however, and we completely failed. We then reverted to our traditional philosophy, and in 1970 we made insider trading a crime.²³ In conformity with our style of legislation, the crime was defined and the punishment provided in a single sentence of twenty-nine lines—in contrast to the British Companies Act of 1980,²⁴ which devotes nine pages to reaching this result. And it works! Obviously, it is impossible to eradicate improper insider trading and tipping in a decade in a country where such activities were a tradition on the part of the most respectable directors and officers, and where tipping was even a social duty, being expected of relatives and friends. The French

²² *Id.* art. 66.

²³ Order No. 67-833 of Sept. 28, 1967, art. 10-1, 1967 D.S.L. 373, 1967 B.L.D. 659, as amended by Statute No. 70-1208 of Dec. 23, 1970, art. 4, 1971 D.S.L. 17, 1971 B.L.D. 17. The provision reads roughly as follows:

Sentence of imprisonment for a period of between two months and two years, and a fine of between 5,000 and 5,000,000 francs, or four times the amount of the profit made, shall be imposed upon [directors and their spouses] as well as any other person having at his disposal, incidentally to the exercise of his profession or function, privileged information on the technical, commercial or financial operation of a corporation, when such persons have carried out on the stock exchange, either directly or through some other person, one or more transactions exploiting the privileged information before the public had knowledge of it.

²⁴ Companies Act of 1980, ch. 22, §§ 68-73.

courts, however, have been able to apply the law without any special difficulty.²⁵ And, if insider trading and tipping have not been completely eradicated, they have ceased to be respectable and have certainly greatly decreased.

If, as a conclusion to this comparative consideration of securities regulation, I may be allowed to express a wish without appearing presumptuous, I shall confess how warmly I wish for you the enactment of the American Law Institute's Federal Securities Code.²⁶ Although American securities law is the most advanced in the world, it is also the most complex and uncertain. The Code offers reasonable and clear solutions with sufficient flexibility to let the courts adjust them in practice. It is true that probably no expert is entirely satisfied with it—probably not even the Reporter himself, Louis Loss. This is, of course, the fate of any compromise document. Hosts of amendments could be offered, but would be challenged. In any case, there is little hope of reaching a better draft or improving the present one. It is also true that the Code may appear to be caught in a wind of deregulation. However, if it is wise after fifty years of social evolution in a certain direction to pause and reconsider one's philosophy, if it is necessary to simplify and coordinate machineries created at different times and for different purposes, then that is precisely what has been done by the drafters of the Code. That is also part of what Dean Freedman advocated in 1978, in his book *Crisis and Legitimacy*,²⁷ to reconcile the American people with their government. And, in this book, which may appear even more important today than when it was published, Dean Freedman singled out the SEC as the most effective of the federal administrative agencies, with the possible exception of the Federal Reserve Board.²⁸

There is always a danger, when an institution has produced satisfactory social results, to believe that those results have been permanently secured and that the institution may now be abolished

²⁵ See Tunc, *Insider Trading in France*, in L. GOWER, L. LOSS & A. SOMMER, *NEW TRENDS IN COMPANY LAW DISCLOSURE* 5 (1980).

²⁶ FEDERAL SEC. CODE (Proposed Official Draft 1978).

²⁷ J. FREEDMAN, *CRISIS AND LEGITIMACY: THE ADMINISTRATIVE PROCESS AND AMERICAN GOVERNMENT* (1978). Compare *THE POLITICS OF REGULATION* (J. Wilson ed. 1980).

²⁸ J. FREEDMAN, *supra* note 27, at 97. See also *id.* 264. It is true that the SEC's performance has more recently been strongly attacked: see H. KRIPKE, *THE SEC AND CORPORATE DISCLOSURE: REGULATION IN SEARCH OF A PURPOSE* (1979). But this attack is directed more to the manner in which the SEC has used its regulatory powers than to the matters covered by the *Federal Securities Code*. Furthermore, Kripke's analysis, useful as it may be in provoking rethinking, has not met with unreserved approval.

or weakened. In fact, any moves towards weakening the institution would permit the social evils to reappear rapidly. Last year, in a symposium on securities regulation in France, I was struck to hear a number of stock exchange officials and members of the financial community complaining about the power exercised by the COB, and arguing that their practices had greatly changed in recent years. I could not help remarking that their practices had changed precisely because of the COB's pressure and that there is no guarantee that these changes would remain in place if the COB's surveillance were relaxed.²⁹ I hope that you Americans will avoid the trap of excessive deregulation and that the Code, the fruit of so many efforts by some of the best experts of the country, will not be set aside lightly or modified in any substantial way.

II. CORPORATION LAW

If, in the field of securities regulation, we have followed your path sometimes slavishly, in the field of corporation law, on the contrary, we have hardly anything in common. The French lawyer who reads, for example, the General Corporation Law of Delaware³⁰ or even the Model Business Corporation Act,³¹ may find them nearly empty on fundamental questions, or at least extraordinarily permissive. Conversely, an American lawyer reading our 1966 Law³² and our 1967 Decree³³ will conclude that they have been drafted by very narrow-minded, suspicious persons who have accumulated petty rules.

Let us compare the provisions regarding payment for shares and the corporation capital. The Model Business Corporation Act (the Model Act) provides: "In the absence of fraud in the transaction, the judgment of the board of directors or the shareholders, as the case may be, as to the value of the consideration received for shares shall be conclusive."³⁴ A 1980 amendment has eliminated the Model Act's section on the determination of the amount of stated capital.³⁵ Professors Frey, Choper, Leech, and Morris, in their excellent *Cases and Materials on Corporations*,³⁶ devote no

²⁹ Tunc, *Aspects des droits étrangers*, LES AUTORITÉS BOURSIÈRES CRÉATRICES DE DROIT 145, 156 (M. Vasseur ed. 1981).

³⁰ DEL. CODE ANN. tit. 8 (1974 & Supp. 1980).

³¹ MODEL BUSINESS CORP. ACT (1980).

³² Statute No. 66-537 of July 24, 1966, 1966 D.S.L. 265, 1966 B.L.D. 353.

³³ Decree No. 67-236 of Mar. 23, 1967, 1967 D.S.L. 137, 1967 B.L.D. 235.

³⁴ MODEL BUSINESS CORP. ACT § 19, ¶ 3 (1980).

³⁵ MODEL BUSINESS CORP. ACT § 21 (1979) (repealed 1980).

³⁶ A. FREY, J. CHOPER, N. LEECH & C. MORRIS, *CASES AND MATERIALS ON CORPORATIONS* 781-82 (2d ed. 1977).

more than a few lines to capital and par value; they underscore how insignificant those concepts now are. Bill Cary and Melvin Aron Eisenberg consider the notion of par value a "vestigial concept."³⁷

In contrast, the notions of capital and par value are basic in French law.³⁸ When our 1966 Act on business organizations³⁹ comes to corporations, it immediately requires them to have a minimum amount of capital. This capital is divided into shares⁴⁰ which must have a minimum par value.⁴¹ The capital must be entirely subscribed.⁴² When shares are issued for cash, at least one quarter of the par value must be paid before issuance,⁴³ and the cash must be deposited with a bank or a notary.⁴⁴ Subscriptions and payments must be formally verified by the incorporators before a notary⁴⁵ (an official much more important—and expensive—than the American notary public) and by a statutory shareholders meeting.⁴⁶ Shares may be paid otherwise than in cash, but not in labor or services. They should then be fully paid before issuance.⁴⁷ The value of property exchanged for shares is assessed by court-appointed experts, whose estimates must be approved by a shareholders meeting.⁴⁸ Does that make sense? Probably not to you. I reserve my judgment.

Take another example: the board of directors. I read in the Model Act⁴⁹ and the Delaware Corporation Law⁵⁰ that the board of directors shall consist of "one or more members." Under French

³⁷ W. CARY & M. EISENBERG, *CASES AND MATERIALS ON CORPORATIONS* 1056 (5th ed. 1980).

³⁸ See Y. GUYON, *supra* note 12, at 109-10, 281-87; 2 J. HAMEL, G. LAGARDE & A. JAUFFRET, *supra* note 14, §§ 396-400, 535-540, 586-611; J. HÉMAR, F. TERRÉ & P. MABILLAT, *supra* note 14, §§ 648-739; 1 R. ROBLOT, *supra* note 12, §§ 1080-1105.

³⁹ Statute No. 66-537 of July 24, 1966, art. 71, 1966 D.S.L. 265, 269, 1966 B.L.D. 353, 360.

⁴⁰ *Id.* art. 73.

⁴¹ *Id.* art. 268.

⁴² *Id.* art. 75. One cannot say without qualification, however, that French law ignores the distinction between issued capital and authorized capital. The shareholders in a general meeting may authorize the board to increase the capital up to a certain amount and this authorization may be valid for five years. *Id.* art. 181, 1966 D.S.L. 275, 1966 B.L.D. 371.

⁴³ *Id.* art. 75.

⁴⁴ *Id.* art. 77; Decree No. 67-236 of Mar. 23, 1967, art. 62, 1967 D.S.L. 137, 141, 1967 B.L.D. 235, 242.

⁴⁵ Statute No. 66-537 of July 24, 1966, art. 78, 1966 D.S.L. 265, 269, 1967 B.L.D. 353, 361.

⁴⁶ *Id.* art. 79.

⁴⁷ *Id.* arts. 75, 80.

⁴⁸ *Id.* art. 80.

⁴⁹ MODEL BUSINESS CORP. ACT § 36 (1980).

⁵⁰ DEL. CODE ANN. tit. 8, § 141 (1974 & Supp. 1980).

law, the board is composed of at least three and at most twelve members.⁵¹ Why is that? We want at least three members in order to prevent the errors or even the misdeeds that could be committed by a single person or even two, and eventually to increase the number of persons who would be subject to criminal or civil liability. We want twelve members at most because to be a nonmanagement director usually involves generous compensation for minimal work, and the temptation would otherwise exist to enlarge the board by providing seats for relatives or friends. For the same reason, no one may be a director of more than eight corporations.⁵² There are, however, some narrow exceptions to these rules.⁵³

To a French lawyer, the Model Act⁵⁴ and the Delaware Corporation Law⁵⁵ seem basically permissive regarding contracts in which directors are financially interested. Our law is much stricter.⁵⁶ Such contracts must first be authorized by the board.⁵⁷ They are then submitted to the *commissaires aux comptes*, who report on them to a general meeting of the shareholders. The shareholders then have the opportunity to approve or disapprove them.⁵⁸ Without entering into details, I only note that six long sections⁵⁹ are devoted to contracts in which a director is financially interested. Once more, I reserve my judgment.

I reserve my judgment because I want to draw your attention to another phenomenon. If an American lawyer were to look at French corporation law, he would also find strange gaps in the law—complete silence on very important points. For instance, we do

⁵¹ Statute No. 66-537 of July 24, 1966, art. 89, 1966 D.S.L. 265, 270, 1966 B.L.D. 353, 362. On the board of directors, see Y. GUYON, *supra* note 12, at 315-50; 2 J. HAMEL, G. LAGARDE & A. JAUFFRET, *supra* note 14, §§ 633-665; 1 J. HÉMAR, F. TERRÉ & P. MABILLOT, *supra* note 14, §§ 794-1042; P. MERLE & E. CHEVALLIER-MERLE, *supra* note 14, §§ 232-276; 1 R. ROBLLOT, *supra* note 12, §§ 1260-1295.

⁵² Statute No. 66-537 of July 24, 1966, art. 92, 1966 D.S.L. 265, 270, 1966 B.L.D. 353, 363.

⁵³ *Id.*; *id.* art. 89.

⁵⁴ MODEL BUSINESS CORP. ACT, § 41 (1980).

⁵⁵ DEL. CODE ANN. tit. 8, § 144 (1974 & Supp. 1980).

⁵⁶ See generally BALENSI, *LES CONVENTIONS ENTRE LES SOCIÉTÉS COMMERCIALES ET LEURS DIRIGEANTS* (1975). The permissiveness of American law should not be exaggerated. In contrast to both the Model Business Corporation Act and Delaware Corporation law, the ABA's guidelines are relatively strict. See CORPORATE DIRECTORS' GUIDEBOOK (rev. ed. 1978), reprinted in 33 BUS. LAW. 1623 (1978).

⁵⁷ Statute No. 66-537 of July 24, 1966, art. 101, 1966 D.S.L. 265, 271, 1966 B.L.D. 353, 364.

⁵⁸ *Id.* art. 103.

⁵⁹ *Id.* arts. 101-06.

not have the doctrine of directors' fiduciary duties. We have, it is true, many rules against the abuses which are prevented in the United States by the doctrine of fiduciary duties. But we do not have the doctrine as such, and this lack of a general philosophy leaves us with serious loopholes. Thus, we have no provision against usurpation of a corporate opportunity. The author of a recent thesis on the subject⁶⁰ has found only one French decision dealing with the problem⁶¹—holding that a director is essentially free to take the corporate opportunity for himself. Thus, we may accuse you of laxity on some points, but we are unquestionably guilty of the same defect on others. Your courts can be very demanding, and even more severe than the English ones,⁶² in imposing fiduciary obligations not only on corporate directors and officers but also on dominant shareholders. A decision such as *Jones v. H.F. Ahmanson & Co.*⁶³ is probably unthinkable in either French or English law.

Thus, if a French lawyer is tempted to believe that your law is the victim of the well-known "race of laxity" denounced by Justice Brandeis,⁶⁴ he must be careful not to jump too fast to a

⁶⁰ J.-Y Martin, *Le Détournement d'une Chance Économique par un Dirigeant de Société (Droits Anglais et Nord-Américains)* (1981) (unpublished thesis, University of Paris I).

⁶¹ Judgment of Nov. 21, 1963, Cour d'Appel, Limoges, 1964 Dalloz, *Jurisprudence* 219 (director who purchased shares in a rival company that was the potential subject of a takeover by his own company not liable for abusing powers of his office).

⁶² Compare *Perlman v. Feldmann*, 219 F.2d 173, 176 (2d Cir. 1955) (fiduciary responsibility of director and majority shareholder includes "dedication of his uncorrupted business judgment for the sole benefit of the corporation") and *Brown v. Halbert*, 271 Cal. App. 2d 252, 272, 76 Cal. Rptr. 781, 793 (1969) (director who was also a majority shareholder breached fiduciary duty to minority shareholders by selling his shares without acting "affirmatively and openly" to provide them a similar opportunity) with *Greenhalgh v. Arderne Cinemas, Ltd.*, [1950] 2 All E.R. 1120, 1126 (majority shareholders who transferred shares in order to breach voting agreement with minority shareholder not liable for any violation of fiduciary duty; test is whether majority believed proposal at issue was for benefit of "individual hypothetical member"). It was not until *Ebrahimi v. Westbourne Galleries, Ltd.*, [1972] 2 All E.R. 492, and the speech of Lord Wilberforce, that English courts began to recognize in a general manner that the exercise of legal rights by a shareholder may be subject to equitable considerations.

⁶³ 1 Cal. 3d 93, 460 P.2d 464, 81 Cal. Rptr. 592 (1969) (majority shareholders owe direct fiduciary responsibility to minority). See generally 83 HARV. L. REV. 1904 (1970).

⁶⁴ *Louis K. Liggett Co. v. Lee*, 288 U.S. 517, 557-59 (1933) (Brandeis, J., dissenting) (footnotes omitted):

The removal by the leading industrial States of the limitations upon the size and powers of business corporations appears to have been due, not to their conviction that maintenance of the restrictions was undesirable in itself, but to the conviction that it was futile to insist upon them Lesser States, eager for the revenue derived from the traffic in charters, had removed safeguards from their own incorporation laws. . . . The race was one not of diligence but of laxity.

definite conclusion. Caution is suggested, in particular, if one observes that a number of French rules had their equivalents in the provisions of nineteenth-century corporation statutes that long ago disappeared from the American scene: minimum capitalization; total subscription; control of payments in kind; stockholders' vote for any important decision and, in particular, for any issue of shares; stockholders' preemptive rights. It is no answer to remark that a number of these rules have recently been introduced in British law by the Companies Act of 1980.⁶⁵ Great Britain had to obey the European Economic Community directives, but did so without any noticeable enthusiasm. Furthermore, one may ask what protection is offered to investors and creditors by the requirement of a fixed and "intangible" capital when, at an annual inflation rate of ten percent, four-fifths of its value is lost in fifteen years.

Thus, while the time approaches for me to reach some conclusion, I find myself full of hesitation. The study of American corporation law gives me, as I told you, great admiration for the depth and the subtlety of your doctrines, judicial decisions, and scholarly writings. At the same time, I am often shocked by the practices revealed in reported cases. Quite often, when my students and I discuss a case, it appears that the defendants' dishonest conduct would have been prevented in France by our rigid rules. I may assure you that, to an outsider, there is a striking contrast between your extremely elaborate, refined, demanding law, aiming at the highest ethical standards, and the grossly dishonest practices which, from your law reports, still seem common, practices which evoke the rough capitalism of the nineteenth century more than the capitalism we are aiming for—practices that would probably be impossible in most other industrialized nations. To choose an example from Pennsylvania, no French promoter could have created a corporation in the incredible manner which appears in *Selheimer v. Manganese Corporation of America*.⁶⁶ The defendants' behavior in this case was possible only because they managed to escape the application of the Securities Act of 1933.⁶⁷ This confirms what has been my long-held belief: if the permissiveness of American corporation law is of little danger to the public from the corporations within the jurisdiction of the SEC, it still permits

⁶⁵ COMPANIES ACT, 1980, ch. 22.

⁶⁶ 423 Pa. 563, 224 A.2d 634 (1966). In *Selheimer*, the officers and majority directors poured money into a plant they knew to be unprofitable, causing a loss to the corporation of approximately \$400,000 in two years. *Id.* at 582-85, 224 A.2d at 645-46.

⁶⁷ 15 U.S.C. §§ 77a-77bbbb (1976).

regrettable conduct on the part of the promoters and managers of closely held or medium-size corporations.

Thus, an outsider is led to fully support Professor Cary's plea for a Federal Corporate Uniformity Act.⁶⁸ I would go even further than him, however presumptuous on my part, and advocate, if not a return to par values, at least some rules on payment for shares in cash. I would also advocate some internal controls on assessing the value of consideration for the issuance of shares when paid in property, labor, or services—assuming that payment in labor or services remains acceptable. The control I advocate is directed toward medium-size corporations. The corporations subject to the SEC's jurisdiction might be exempted from such control. The Manganese Corporation of America, considering the conditions under which it was created and the way it was managed, seems to me the type of corporation that should have been kept under control. The study of your case law leads me to think that many corporations are daily created and managed in the same way, and I am not certain that the trend toward independent boards and board committees will provide a sufficiently effective remedy.⁶⁹

Presumptuous again as it may be on my part, I confess to not being in complete agreement with the conclusions of Professors Brudney and Clark in their recent and remarkable article on corporate opportunities in the *Harvard Law Review*.⁷⁰ You may remember that the authors conclude from their thorough study that the present flexible law is basically suitable for closely held corporations, but that it would be desirable to control the fiduciaries of public corporations with categorical rules. This may be true. The rules proposed by the authors might bring both a higher degree of ethics and a greater degree of certainty, and therefore of security, for directors and managers. What puzzles me are the larger conclusions the authors derive from that first one. Let me quote them at some length:

We think that the formulation of corporate law doctrines by state courts has been *pervasively* influenced by the fact that the overwhelming majority of corporate cases coming

⁶⁸ See Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L.J. 663, 701-03 (1974). See also M. EISENBERG, *THE STRUCTURE OF THE CORPORATION: A LEGAL ANALYSIS* 329-30 (1976); Young *Federal Corporate Law, Federalism, and the Federal Courts*, 41 LAW & CONTEMP. PROBS. 146 (1977).

⁶⁹ For a discussion on this point, see Ruder, *Current Issues Between Corporations and Shareholders: Private Sector Responses to Proposals for Federal Intervention Into Corporate Governance*, 36 BUS. LAW 771, 775-77 (1981).

⁷⁰ Brudney & Clark, *A New Look at Corporate Opportunities*, 94 HARV. L. REV. 997 (1981).

before state courts have involved close corporations. It is widely noted, of course, that the earlier state statutory rules, which upon analysis seem geared to the paradigm of the public corporation, impose rigidities that had to be struggled with and modified by courts and legislators to accommodate the needs of close corporations. But we believe that the press of close corporation cases has had an equally great, albeit inappropriate, effect on rules governing public corporations: with respect to a number of important doctrines, the judicially developed rules of *general* applicability to all corporations are more suited to close corporations.⁷¹

I do not contest the description of the historical development as presented by Professors Brudney and Clark. Perhaps it is also true in general, and not only as regards corporate opportunities, that some hard and fast rules would impose on corporate fiduciaries a still higher degree of ethics and at the same time relieve them of the current uncertainty of the law. However, I assume that most public corporations, because they are subject to federal legislation, are managed in a manner which is legally satisfactory. What worries me is the medium-size corporation: the corporation whose directors escape the personal ties described by Professors Brudney and Clark as characteristics of the close corporation and also escape federal legislation and the SEC's control. If it is true that your law presents serious gaps on the level of the medium-size corporation, and if you feel that a Federal Corporate Uniformity Act is appropriate, then perhaps you might look with profit to some of the rules, archaic as they may appear to you at first blush, of some other industrialized countries.

You might even consider some new experiments that could inspire an improvement of your law. For instance, Professor Gower has wisely remarked that one problem with derivative actions is that a shareholder lacks the precise information that would enable him to bring a useful lawsuit. Disclosure, "though it may enable a stockholder to detect the symptoms of sickness in the corporate body . . . is not likely to show him the cause of the ailment," nor to "provide him with the evidence which he needs to bring a lawsuit."⁷² British legislation has tried to remedy the situation by conferring upon the Department of Trade power to appoint an inspector to investigate the affairs of a company⁷³ and, more re-

⁷¹ *Id.* 1061-62 (footnote omitted).

⁷² Gower, *supra* note 6, at 1387.

⁷³ COMPANIES ACT, 1948, 11 & 12 Geo. 6, ch. 38, §§ 164-166, §§ 164-175.

cently, power to inspect a company's books and papers.⁷⁴ For a number of reasons, however, the Department of Trade is not very effective in this regard.⁷⁵ The SEC sometimes conducts very thorough investigations. But it does so only when it suspects a violation of the law, not mere incompetence; when a corporation is subject to its jurisdiction; and when a corporation attracts its attention.

These limitations suggest the potential of a device introduced in France by the 1966 Act.⁷⁶ One or more shareholders holding at least one-tenth of the capital may, by a very swift and inexpensive procedure (*référé*), request the court to appoint an expert whose duty will be to investigate and report on one or more transactions by the corporation (*opérations de gestion*). Such a report is sent to the petitioners and to the board, and through the auditors (*commissaires aux comptes*), distributed to all shareholders. The terms of reference of the expert, currently called the minority expert (*l'expert de la minorité*), may be very broad, including not only findings of fact, but also opinions on the legality and the propriety of what has been done. His report may thus be extremely valuable to the shareholders. It enables them to appreciate the advisability not only of bringing a derivative action, but also of dismissing one or more directors or appointing a new board, or exercising any of the rights granted to shareholders, individually or collectively, by our legislation.⁷⁷ A government bill, which failed during the last legislature but which will probably be reintroduced and passed by the present one, would extend the power of requesting an *expertise de minorité* to the *commissaires aux comptes*,⁷⁸ the public prosecutor (*ministère public*),⁷⁹ and the COB.⁸⁰

⁷⁴ COMPANIES ACT, 1967, ch. 81, §§ 109-118.

⁷⁵ L. GOWER, PRINCIPLES OF MODERN COMPANY LAW 671-80 (4th ed. 1979).

⁷⁶ Statute No. 66-537 of July 24, 1966, art. 226, 1966 D.S.L. 265, 278, 1966 B.L.D. 353, 376; Decree No. 67-236 of Mar. 23, 1967, art. 195, 1967 D.S.L. 137, 149, 1967 B.L.D. 235, 256. See also Y. GUYON, *supra* note 12, at 448; 2 J. HAMEL, G. LAGARDE & A. JAUFFRET, *supra* note 14, 680; 2 J. HÉMAR, F. TERRÉ & P. MABILAT, *supra* note 14, §§ 1064-1082; MERLE & CHEVALLIER-MERLE, *supra* note 14, §§ 335-356; 1 R. ROBLLOT, *supra* note 12, § 1341; Boy, *Réflexions sur le sort de l'expertise de minorité*, 1980 Dalloz, *Chroniques* 79.

⁷⁷ On these rights, see Y. GUYON, *supra* note 12, at 443-65; L. SCHMIDT, *LES DROITS DE LA MINORITÉ DANS LA SOCIÉTÉ ANONYME* (1970).

⁷⁸ On the *commissaires aux comptes*, see *supra* note 14 and accompanying text.

⁷⁹ A typically French institution, the *ministère public* is composed of a special category of judges in charge of promoting and presenting the public interest before the courts. See R. DAVID & J. BRIERLEY, *MAJOR LEGAL SYSTEMS IN THE WORLD TODAY* §§ 103, 335 (2d ed. 1978); A. VON MEHREN & J. GORDLEY, *THE CIVIL LAW SYSTEM* 144-46 (2d ed. 1977).

⁸⁰ On the COB, see *supra* text accompanying notes 11-12.

Regarding the derivative action, I may mention incidentally that our legislation completely rejects the doctrine of exhaustion of internal remedies and the notion that disinterested directors can terminate a derivative suit if they conclude it is not in the best interests of the shareholders.⁸¹ Rather, it treats the derivative action as an individual right granted to shareholders. The plaintiff who brings a derivative suit need not notify or secure the authorization of the other shareholders.⁸² Nor can a derivative suit be blocked by a majority of the shareholders. Any authority of the board to block such a suit is denied *sub silentio*.

III. PARTING THOUGHTS

Finally, I would like to list a number of recent phenomena that worry me and for which I do not see any solutions.

(1) The thirst for technological progress entails sudden changes in the value of shares. The announcement of a new product or a new process can cause a stock market quotation to jump. A few weeks later, some defects or difficulties may appear or a competitor may market another product, and the quotation will fall as sharply.

(2) The suddenness of change is, of course, greatly increased by the role played in the stock market by institutional investors. Within a few hours, institutional investors can buy or sell hundreds of thousands of shares before the individual investor even learns of the news that has prompted their decision. In such an environment, the fate of the individual investor has been compared to that of an infantryman lost in a battle of armored tanks.

(3) The main purpose of disclosure—a basic philosophy of your federal law—is to enable the investor to make an informed choice.⁸³ Until recently, however, this philosophy of disclosure

⁸¹ See *Burks v. Lasker*, 441 U.S. 471, 485 (1979) (disinterested directors may terminate nonfrivolous suit brought under Investment Company and Investment Advisers Acts of 1940, if they reasonably believe suit is not in best interests of shareholders). *Accord*, *Zapata Corp. v. Maldonado*, 430 A.2d 779, 786-88 (Del. 1981). See generally *Coffee & Schwartz, The Survival of the Derivative Law Suit: An Evaluation and a Proposal for Legislative Reform*, 81 COLUM. L. REV. 261 (1981).

⁸² Statute No. 66-537 of July 24, 1966, art. 246, 1966 D.S.L. 265, 279, 1966 B.L.D. 353, 378. For commentary on American derivative action suits, see W. CARY & M. EISENBERG, *supra* note 37, at 917-35; A. FREY, J. CHOPER, N. LEECH & C. MORRIS, *supra* note 36, at 659-85; H. HENN, *HANDBOOK OF THE LAW OF CORPORATIONS & BUSINESS ENTERPRISES* 770-75 (2d ed. 1970); D. VAGTS, *BASIC CORPORATION LAW: MATERIALS, CASES, TEXT* 450-525 (1973).

⁸³ For a general questioning of the assumptions underlying the American policy of disclosure, see H. KRIPKE, *supra* note 28.

rested on the assumption that past performance would be more or less reproduced in the future. Now, at a time of rapid economic and technological change, this assumption is less valid. More broadly, under the disclosure approach, accounts giving a true and fair view of the accomplishments and situation of the corporation are considered the basis of the investor's protection. Such accounts, however, have never been entirely accurate; the amount of depreciation to be taken has traditionally been a business decision. But the uncertainty of the accounts has greatly increased in the last years, not only as a result of inflation, but also as a result of technological progress. A machine may be expected to work properly for fifteen years, but become valueless within a few years. How many? Nobody knows—because a new energy-saving or work-saving machine may be available. Under such circumstances, the accounts, notwithstanding recent efforts to introduce new methods of accounting, are much less informative than they were in the past. Soft and projective information is desirable, but it may be misleading, even if developed in good faith, and it is extremely difficult to regulate. Perhaps only highly qualified and specialized analysts working with computers can make use of information with a certain degree of safety. Because such analysts are small in number and give advice primarily to institutional investors, the fate of the individual investor appears more and more bleak.

(4) Thus, it may appear safer for the individual investor not to take risks in the stock market himself but to seek refuge in a mutual fund. This decreases the social utility of the stock market, however, because most mutual funds can only invest in large corporations and do not contribute to financially promising but smaller corporations. Furthermore, there is no need to recall here the losses incurred in recent decades by participants in mutual funds, even in funds managed by prestigious financial institutions. Anyone can be wrong. When Penn Central went bankrupt in 1970, thirteen insurance companies held bonds totalling \$500 million, which lost four-fifths of their value. In 1977, the IBM Corporation considered it a good investment to repurchase four million of its shares at \$280 per share. After a four for one split, the shares are presently quoted at well below \$70 per share in current dollars. In the meantime, IBM has been obliged to borrow heavily at a high rate of interest. As for the individual investor, running from a mutual fund that has performed brightly one year to another that performed better the following year, he may be running from disappointment to disappointment.

Professor Clark is probably right in observing that the concentration of wealth in the hands of institutional investors and the concentration of expertise among a handful of securities analysts has led capitalism to a new stage.⁸⁴ I personally have the greatest difficulty seeing what effective protection can be given to the ordinary citizen to permit and encourage him to invest safely in securities. But you Americans have shown yourselves to be so resourceful in facing new situations that I feel sure you will devise proper solutions, and that it will remain both exciting and profitable for a foreigner to look at American corporation law and securities regulation.

⁸⁴ Clark, *The Four Stages of Capitalism: Reflections on Investment Management Treatises*, 94 HARV. L. REV. 561 (1981).